IN THE HIGH COURT OF JUDICATURE AT MADRAS

DATED: 25.10.2006

CORAM

THE HON'BLE MR.JUSTICE P.D.DINAKARAN
AND
THE HON'BLE MR.JUSTICE P.P.S.JANARTHANA RAJA

T.C.(A) No.2400 of 2006

Commissioner of Income Tax
Chennai. .. Appellant/Respondent

Vs

The Tamil Nadu Small Industries
Development Corporation
1, Paulawala Road
Kathipara Junction, Guindy
Chennai-600 015. .. Respondent/Appellant

PRAYER: Appeal under Section 260A of the Income Tax Act, 1961 against the order of the Income Tax Appellate Tribunal, 'B' Bench, Chennai dated 30.06.2005 in I.T.A.No. 494/Mds/2000 for the assessment year 1993-94 against the order of the Commissioner of Income Tax (Appeals) Chennai 600 034 dated 2.12.99 in ITA.No.8/99-2000 against the Joint Commissioner of Income Tax Special Range III Chennai 600 034, dated 12.3.99 and made in PAN/GIR.No.3T for the Asst year 1993 - 94.

For Appellant : Mr.T.Ravi Kumar

J U D G M E N T

(Delivered by P.D.DINAKARAN,J.)

The above tax case appeal is directed against the order of the Income-tax Appellate Tribunal dated 30.06.2005 made in I.T.A.No.494/Mds/2000 for the assessment year 1993-94, setting aside the orders of the authorities below.

2.1. The facts in a nutshell are that the assessee, a company wholly owned by the State Government, filed its return of income for the assessment year 1993-94 admitting an income of Rs.49,40,823/-, and the assessment was completed under Section 143(3) of the Income Tax Act on a total income of

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Rs.56,19,300/-. On noticing that some income escaped assessment, a notice under Section 148 of the Act was issued to the assessee, who filed a revised return admitting the income as per the original return, viz., Rs.49,40,823/-. The assessing officer, finding that though the assessee followed mercantile system of accounting, only with respect to the interest received on deposits from M/s.Andhra Bank Financial Services Ltd. the assessee followed cash system of accounting, treated the interest accrued during the relevant period as income on mercantile basis.

2.2. On appeal, before the Commissioner of Income Tax (Appeals), the assessee submitted that the interest on deposit with M/s.Andhra Bank Financial Services Ltd., has not accrued to the assessee company since the principal was in doubt and for that reason alone, the assessee company has been accounting for the interest on receipt basis. But, the Commissioner of Income Tax (Appeals), taking note of the order of the CIT(A)-III dated 9.3.1998 in I.T.A.No.95/96-97, for the assessment year 1994-95, confirming the addition of interest accrued on the amount due from M/s.Andhra Bank Financial Services Ltd., upheld the addition of Rs.40 Lakhs being interest accrued and receivable from M/s.Andhra Bank Financial Services Ltd., for the assessment year 1993-94 and confirmed the order of the Assessing Officer.

2.3. On further appeal by the assessee, the Tribunal, taking note of its orders in the assessee's own case for the assessment years 1994-95 and 1995-96 and also the judgment of this Court in CIT v. Pondicherry Industrial Promotion Development Investment Corporation Ltd., [2002] 254 ITR 748, wherein it is held that cash system of accounting can be followed insofar as the interest and rent are concerned, held that the assessee is entitled to follow cash system of accounting with regard to interest, thereby setting aside the orders of the authorities below and upholding the claim of the assessee.

2.4. Hence, the present appeal by the Department raising the following substantial questions of law:

(i) Whether on the facts and circumstances of the case the Tribunal was right in holding that interest from Andhra Pradesh Financial Corporation should be taxed only on cash basis, while the assessee was following mercantile system of accounting? And

(ii) Whether on the facts and circumstances of the case the Tribunal was right in applying the ratio of the decision of this Court in the case of Pondicherry Industrial Promotion Development Investment Corporation Ltd., [2002] 254 ITR 748?

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3. The main argument of the learned Counsel for the Revenue is that since it is agreed by M/s.Andhra Bank Financial Services Ltd. that interest would be paid to the assessee after paying the principal amount due to them, it should be construed that the interest is actually received by the assessee.

4. It is the case of the assessee that the interest on deposit with M/s.Andhra Bank Financial Services Ltd., has not accrued to the assessee company since the principal was in doubt, and that M/s.Andhra Bank Financial Services Ltd. defaulted in the payment of interest during the financial year 1992-93 and therefore, from that year onwards the assessee company has been accounting for the interest on receipt basis.

5. When an issue regarding hybrid accounting came up before the Apex Court in UCO Bank v. CIT, [1999] 237 ITR 889, wherein the assessee while following the mercantile system of accounting considered the income by way of interest pertaining to doubtful loans as not real income in the year in which it accrued, but only when it was realised, the Apex Court held that such a mixed system of accounting was in accordance with the accounting practice.

6. This Court in Commissioner of Income-tax v. Pondicherry Industrial Promotion Development Investment Corporation Ltd., [2002] 254 ITR 748, having regard to the decision of the Apex court, referred supra, that it cannot be said that it was impermissible for the assessee to have followed a mixed or a hybrid system of accounting and that while following the mercantile system, it was permissible for it to adopt a cash system of accounting so far as interest and rent were concerned, held that the assessee cannot be held to be disentitled to change the method of accounting even when it is genuine solely on the ground that such a mixed system of accounting would result in loss to the Revenue for that year.

7. The ratio laid down in the decisions referred supra, is squarely applicable to the facts and circumstances of the case on hand. Finding therefore no substantial question of law, this appeal is dismissed.

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Sd/
Asst.Registrar

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Sub Asst.Registrar

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To:

1. The Assistant Registrar,
   Income-tax Appellate Tribunal, 'B' Bench
   Rajaji Bhavan, Besant Nagar, Chennai 600 090.

2. The Commissioner of Income-tax (Appeals), XII
   Chennai.34

3. The Commissioner of Income Tax
   Tamil Nadu-III, Chennai.

4. The Joint Commissioner of Income Tax Special Range III,
   Chennai 600 034.

5. The Commissioner of Income Tax, Chennai.

+ 1 cc to Mr. Pushya Sitaraman, Advocate SR No. 49863

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